

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 SSO-00 NSCE-00 USIE-00 INRE-00

AID-05 CEA-01 CIAE-00 COME-00 EB-07 EA-06 FRB-03

INR-07 IO-10 NEA-09 NSAE-00 OPIC-03 SP-02 TRSE-00

CIEP-01 LAB-04 SIL-01 OMB-01 ERDA-05 DODE-00 FEAE-00

FPC-01 H-02 INT-05 L-02 NSC-05 PM-03 SAM-01 OES-03

SS-15 STR-04 PRS-01 PA-01 AF-06 ARA-06 /133 W

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O 221841Z APR 75

FM USMISSION OECD PARIS

TO SECSTATE WASH DC IMMEDIATE 6706

C O N F I D E N T I A L SECTION 01 OF 02 OECD PARIS 10260

FOR FSE (BOSWORTH)

E.O. 11652: GDS

TAGS: ENRG, OECD

SUBJECT: IEA: BACKGROUND DOCUMENTS FOR APRIL 28-30

SLT MEETING

BEGIN TEXT

PROTECTION OF THE VALUE OF THE COMMON MINIMUM PRICE
IN REAL TERMS

IN ORDER TO BE EFFECTIVE, THE COMMON MINIMUM PRICE WILL
HAVE TO BE ENVISAGED IN REAL TERMS SO AS TO BE PROTECTED
AGAINST FUTURE INCREASES OF PRODUCTION COST OF ALTERNA-
TIVE ENERGY SOURCES. THIS COULD BE DONE IN THREE WAYS:

(A) AUTOMATIC ADAPTATION EX ANTE, BASED ON SOME
COMMONLY AGREED FACTOR TO TAKE ACCOUNT OF
EXPECTED INCREASES IN PRODUCTION COST;

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(B) AUTOMATIC ADAPTATION EX POST, BASED ON INCREASES IN PRODUCTION COST, AFTER THESE ARE REALIZED;

(C) PERIODIC REVIEW.

THE ADVANTAGE OF BOTH FORMS OF AUTOMATIC ADAPTATION IS THAT IT WOULD GIVE POTENTIAL INVESTORS MORE CERTAINTY ABOUT THE FUTURE LEVEL OF THE COMMON MINIMUM PROTECTED INFLATION, SINCE THERE MAY BE LESS INCENTIVE TO KEEP INCREASES IN PRODUCTION COSTS DOWN.

THE ADVANTAGE OF AUTOMATIC ADAPTATION EX POST IS THAT IT SEEMS TO BE A MUCH MORE PRECISE INSTRUMENT IN SO FAR AS INCREASES IN PRODUCTION COST MAY BE QUITE DIFFICULT TO FORESEE BECAUSE OF THE UNCERTAINTY OF SOME OF THE FACTORS INVOLVED (PRICES OF STRUCTURAL STEEL AND LINE-PIPE HAVE DOUBLED SINCE EARLY 1973; PRICES OF CEMENT STARTED RISING DRAMATICALLY IN MID-1974). THE DISADVANTAGE OF AUTOMATIC ADAPTATION EX POST, HOWEVER, IS THAT ADAPTATION WOULD ONLY TAKE PLACE SOME TIME (ABOUT 1 YEAR) AFTER PRODUCTION COST INCREASES HAVE TAKEN PLACE AND WOULD THEREFORE TEMPORARILY REDUCE THE EFFECTIVE PROTECTION BY THE AMOUNT OF THE PRODUCTION COST INCREASES.

IN THE LIGHT OF THE FOREGOING IT SEEMS THAT A COMBINATION OF AUTOMATIC ADAPTATION EX ANTE AND EX POST WOULD BE BEST SET FOR GIVING THE NEEDED PROTECTION TO THE INVESTORS, WHILE ENABLING AT THE SAME TIME TO TAKE ACCOUNT OF THE INCREASES IN PRODUCTION COSTS WHICH HAVE TAKEN PLACE. IN THIS SYSTEM THE COMMON MINIMUM PRICE OF IMPORTED OIL WOULD BE ADAPTED AUTOMATICALLY FOR THE COMING YEAR WITH SOME COMMONLY AGREED FACTOR TO BE CORRECTED AT THE BEGINNING OF THE NEXT YEAR FOR THE INCREASES IN PRODUCTION COST WHICH HAVE TAKEN PLACE IN REALITY.

DURATION OF THE SCHEME:

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A MAJOR PROBLEM IN CONNECTION WITH THE SCHEME IS THE APPARENT CONTRADICTION BETWEEN THE MINIMUM DURATION WHICH WOULD ENCOURAGE INVESTMENTS IN THE DEVELOPMENT OF ALTERNATIVE ENERGY SOURCES, AND THE MAXIMUM POSSIBLE DURATION IN THE FRAMEWORK OF THE AGREEMENT ON THE INTERNATIONAL ENERGY PROGRAM.

AN EXAMPLE TO ILLUSTRATE THE MINIMUM DURATION FROM THE

VIEWPOINT OF INVESTING COMPANIES IS THE DEVELOPMENT OF A LARGE NORTH SEA OIL FIELD WHICH WOULD TAKE A LEAD-TIME OF NINE OR TEN YEARS FROM DISCOVERY TO DEVELOPMENT AND ANOTHER SEVEN YEARS FROM THE START OF DEVELOPMENT FOR AN OPERATOR TO SEE A POSITIVE CASH-FLOW. THIS SHOULD BE COMPARED WITH THE POSSIBLE DURATION IN THE FRAMEWORK OF THE AGREEMENT (TEN YEARS WITH A MAJOR REVIEW AFTER THE FIRST FIVE YEARS).

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THERE ARE AT LEAST TWO ALTERNATIVE SOLUTIONS TO THIS PROBLEM. A FIRST WOULD BE TO EXTEND THE DURATION OF THE SCHEME BEYOND THE DURATION OF THE AGREEMENT, EITHER BY INCORPORATING THE SCHEME IN A SEPARATE AGREEMENT OUTSIDE THE FRAMEWORK OF THE IEA, EITHER BY WAY OF A GOVERNING BOARD DECISION, WHICH WOULD EXPLICITLY STIPULATE THAT THE SCHEME WOULD SURVIVE THE DURATION OF THE

AGREEMENT AND/OR THE WITHDRAWAL OF PARTICIPATING COUNTRIES FROM THE AGREEMENT.

A SECOND SOLUTION WOULD BE TO LIMIT THE AGREEMENT ON THE SCHEME TO THE DURATION OF THE IEA AGREEMENT (10 YEARS WITH A MAJOR REVIEW AFTER FIVE YEARS) BUT TO SUPPORT THE SCHEME BY ADDITIONAL SPECIAL MEASURES TO ENCOURAGE INVESTMENTS IN ALTERNATIVE ENERGY SOURCES IN IEA COUNTRIES, FOR EXAMPLE BY WAY OF SOME INTERNATIONAL INVESTMENT GUARANTEE SCHEME.
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IN ADDITION TO THE TWO ALTERNATIVES JUST MENTIONED, OTHER SOLUTIONS COULD BE CONSIDERED, AS MAY BECOME EVIDENT FROM THE FOLLOWING ENUMERATION, WHICH STARTS WITH THE ALTERNATIVE GIVING THE GREATEST INCENTIVE TO INVESTORS TO GO DOWN TO THE ALTERNATIVE LEAVING THE GREATEST FLEXIBILITY TO GOVERNMENTS:

(A) AN INDEPENDENT AGREEMENT FOR THE ESTABLISHMENT OF A GENERAL SCHEME FOR A COMMON MINIMUM PROTECTED PRICE FOR IMPORTED OIL WITH A DURATION OF 15-20 YEARS, COMBINED WITH THE ESTABLISHMENT OF SUPPORTING SPECIFIC MEASURES SUCH AS AN INTERNATIONAL INVESTMENT GUARANTEE SCHEME (NO POSSIBILITY TO REVIEW THE SCHEME);

(B) (A) WITHOUT SUPPORTING SPECIFIC MEASURES;

(C) (A) WITHOUT SUPPORTING SPECIFIC MEASURES AND WITH THE POSSIBILITY TO REVIEW THE SCHEME AFTER 5 OR 10 YEARS;

(D) THE ESTABLISHMENT OF A SCHEME FOR 10 YEARS (DURATION OF THE AGREEMENT), SUPPORTED BY SPECIFIC MEASURES, NO REVIEW;

(E) (D) WITHOUT SUPPORTING SPECIFIC MEASURES;

(F) (D) WITHOUT SUPPORTING SPECIFIC MEASURES AND WITH REVIEW;

(G) THE ESTABLISHMENT OF A SCHEME FOR ANY PERIOD SHORTER THAN 10 YEARS. END TEXT

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